FILED
JUL 1 1942
CHARLES ELMORE CROPLEY
CLERK

No. 195

In the

Supreme Court of the United States

October Term, 1942

AMERICAN LIBERTY OIL COMPANY, *Petitioner,*

vs.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

JOHN BARRE KING,
Counsel for Petitioner.

E. Duncan & Co., Brief Printers, Dallas

SUBJECT INDEX

	Page
Petition for a Writ of Certiorari	1 - 7
Summary Statement of the Matter Involved	2 - 4
Issues Presented	4 - 5
Reasons for Review	5 - 6
Prayer for Writ	6 - 7
Brief in Support of Petition for a Writ of Certiorari	8 - 17
Opinions Below	8
Jurisdiction	8 - 9
Statement of Facts	9
Specifications of Error	9
Argument	10 - 16
Conclusion	17

TABLE OF CASES CITED

American Liberty Oil Company, 43 B. T. A. 76-127, Fed. (2d) 262	2, 8
Burnet vs. Logan, 283 U.S. 404	4, 10
Columbia Oil and Gas Co. vs. Commissioner, 118 Fed. (2d) 459	13
Montrose Cemetery Co. vs. Commissioner, Fed. (2d) 238	14
Ortiz Oil Co. vs. Commissioner, 37 B. T. A. 656	12
E. F. Simms vs. Commissioner, 28 B. T. A. 988	13

In the

Supreme Court of the United States

October Term, 1942

AMERICAN LIBERTY OIL COMPANY, *Petitioner*,

vs.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioner, American Liberty Oil Company, respectfully represents as follows:

This is a petition for a writ of certiorari to review the judgment of the United States Circuit Court of Appeals for the Fifth Circuit, which, in all material issues involved in this petition, affirmed a decision of the United States Board of Tax Appeals, but which remanded the case to the United States Board of Tax Appeals with direction

to recompute the tax on an issue not important to this petition.

The opinion and judgment of the Circuit Court of Appeals was rendered on April 3, 1942 and is reported in 127 Fed., (2d, p. 262)

I.

Statement

The petitioner, American Liberty Oil Company, is a Delaware corporation. It owned a considerable number of leases located in what is known as the East Texas oil fields. In May, 1934 the petitioner sold these leases to the Atlantic Oil Producing Company together with all equipment situated thereon. (R. 116-162)

It reserved and accepted from the sale, however, 4,400,00 barrels of oil *when, as and if produced*, which reservation was subject to certain oil payments theretofore reserved by third parties aggregated $1,206,391.17.

The respondent, as of January 1, 1934, estimated the oil reserves in and under these leases as being 19,295,522 barrels, and at the date of the sale there was, according to the respondent, oil reserves to the amount of 19,089,603 barrels.

The facts in this case were in the main stipulated, and, according to the stipulation of facts, the petitioner received $1,500,000 in cash. At the time of the sale it had a depre-

ciated cost of well equipment of $648,134.05 and a leasehold cost less depletion allowed or allowable of $469,828.01. Petitioner also incurred legal expenses, commissions and cost of abstracts amounting to $19,149.96.

From the stipulated facts it therefore appears that the cash consideration of $1,500,000 was not equal to the depreciated and depleted cost of $1,614,122.02 and that, if petitioner was to realize a profit from this transaction, it must realize it from the 4,400,000 barrels of oil reserved *when, as, and if produced.* (See Stipulation of facts, R. 108-112 inclusive.)

Notwithstanding this fact, the respondent in his notice of deficiency determined that petitioner realized a net profit of $706,780.16 In so doing the respondent valued the oil reserved at fifty cents on the dollar and allocated both lease equipment and leasehold costs to the cash received and to the valuation he had placed on the oil reservation. (R. 112)

The Board of Tax Appeals and, in this respect, the Circuit Court of Appeals held that no part of the lease equipment cost should be allocated to the oil reservation and we have no fault to find with opinions in this particular.

Both the Board of Tax Appeals and the Circuit Court, however, held contrary to petitioner regarding what we shall call the "Tyler Pipe Line Company question." This was the only issue that was not stipulated and the facts,

as petitioner sees them, are that in order to consummate the sale to the Atlantic Oil Producing Company, the petitioner was forced to pay $120,000 to the Tyler Pipe Line Company to obtain a release from a contract it had previously made with the Tyler Company. It is true that the amount of the payment was not agreed upon and the actual payment did not occur until 1936, but when the evidence is examined, it will be seen that this payment was necessary in order to consummate the transaction. There was, in fact, no dispute as to the liability, the only dispute being as to the amount. (R. 167-169.)

Stated as succinctly as petitioner can do so, these represent the material facts and apprize the court of the issues involved.

II.

The issues presented by this petition are:

FIRST: According to the stipulated facts, petitioner received from the sale of these leases $1,500,000 in cash. It had expended in excess of $1,614,000. Its only opportunity to recoup its capital investment was from oil reservations which might or might not materialize or, as this Court said in *Burnet vs. Logan*, 283 U. S. 404, "the promise of future money payments were wholly contingent upon thing like fair certainty." Is not therefore the act of the respondent in allocating a portion of the leasehold cost to these oil reservations, which may or may not be realized, in

effect a tax imposed on capital and should not the profit be postponed until the "wholly contingent" possibility be realized?

SECOND: Bearing in mind that the reservation was so much oil and not so much money payable out of oil, can it be said that the Circuit Court of Appeals was correct in making its allocation on the basis of the market price of the oil reserved rather than an allocation on the basis that the oil reserved bore to the oil sold?

THIRD: It is not a fact that where a seller must expend a certain amount of money in order to consummate a sale, that the amount paid (whether then determined or determined at a later date) constitutes a part of its cost and doesn't it follow that where this cost is disregarded, the imposition of the tax, *without regard to the amount paid*, is a tax on capital rather than on income to the extent of such payment?

Reasons for Review

1. The decision of the Uinted States Circuit Court of Appeals for the Fifth Circuit is in direct conflict with the decision of this court in the case of *Burnet vs. Logan*, 283 U. S. 404. In the case cited this Honorable Court laid down the rule that where a taxpayer may never recoup its full cost because the future payments out of oil were "wholly contingent upon facts and circumstances not possible to fortell with anything like fair certainty," is a tax on

capital rather than upon income. This meets our case exactly because under the stipulated facts petitioner received $1,500,000 in cash and had expended in excess of $1,614,000 in cash.

2. In passing upon this case the Circuit Court of Appeals for the Fifth Circuit has decided an important question of federal law which has not been, but should be settled by this Court (if in fact a portion of the leasehold cost should be allocated to the oil reserved), then this Court should lay down a rule which would govern all other Circuit Courts of Appeals.

It is such an important question of federal law that it should be settled by this court.

WHEREFORE Your petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the United States Circuit Court of Appeals for the Fifth Circuit, commanding that court to certify and to send to this court for its review and determination on a day certain to be therein named, a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket No. 10,108, American Liberty Oil Company, petitioner, vs. Commissioner of Internal Revenue, respondent, and that the judgment of the United States Circuit Court of

Appeals for the Fifth Circuit may be reversed, and that your petitioner may have such other and further relief in the premises as this Honorable Court may deem mete and just, and your petitioner will ever pray.

AMERICAN LIBERTY CIL COMPANY,

By

JOHN BARRE KING,
Counsel for Petitioner.